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August 15, 1997

William F. Caton, Acting Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area (CC Docket No. 96-149);

Policy and Rules Concerning the Interstate, Interexchange Marketplace (CC Docket No. 96-61);

Leaco Rural Telephone Cooperative, Inc.; Petition for waiver

Dear Mr. Caton:

Transmitted herewith, on behalf of Leaco Rural Telephone Cooperative, Inc., are an original and four copies of the above-referenced Petition for Waiver. Should the Commission have any questions or require additional information, it is respectfully requested to contact the undersigned.

Very truly yours,

Michael R. Bennet

Michael R. Bennet

Enclosures

cc: Andrea Kearney

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington D.C. 20554

In the Matter of	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area	)))	**CC Docket No. 96-149**
	)	
and	)	
	)	
Policy and Rules Concerning the Interstate, Interexchange Marketplace	))	**CC Docket No. 96-61**

To: Common Carrier Bureau

Petition for Waiver

Leaco Rural Telephone Cooperative, Inc. ("Leaco"), pursuant to Section 1.3 of the Rules and Regulations of the Federal Communications Commission ("FCC" or "Commission"), hereby requests a waiver of the existing separation requirements established by the Commission in its *Competitive Carrier Fifth Report and Order*.[1] These separation requirements are currently a

[1] *See* Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefore, CC Docket No. 79-252; Fifth Report and Order, 98 FCC 2d 1191 (1984) (*"Fifth Report and Order"*). In the *Fifth Report and Order*, the Commission determined that, in order to qualify for non-dominant treatment, an independent LEC must provide interstate and international interexchange services through an affiliate and that such affiliate must : "(1) maintain separate books of account; (2) not jointly own transmission or switching facilities with its affiliate exchange telephone company; and (3) acquire any services from its affiliated exchange telephone company at tariffed rates, terms and conditions. The FCC recently adopted an order codifying and partially modifying these separation requirements. *See* Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area; Policy and Rules Concerning the Interstate, Interexchange Marketplace, *Second Report and Order* (CC Docket No. 96-149) and *Third Report and Order* (CC Docket No. 96-61), FCC 97-142 (released April 18, 1997) (collectively, *"Separate Affiliate Order"*).

(continued...)

prerequisite for independent local exchange companies ("LECs") to qualify as non-dominant carriers in the provision of interstate, domestic and international interexchange services originating in their local exchange areas. The Commission has stated that "[t]o the extent that special circumstances exist, however, independent LECs may petition us to establish the necessity of a waiver of the *Fifth Report and Order* requirements." *Separate Affiliate Order* at ¶ 173. In Leaco's case, special circumstances exist which support a waiver of the requirement that Leaco comply with these separation requirements in order to obtain non-dominant status for its interstate and international long distance resale operations. Herein, Leaco provides *specific evidence* of the increased financial burden that will be imposed on both Leaco and its customers by enforcement of the separate affiliate requirement.

I. Background

Leaco is a cooperative local exchange company providing service in eastern New Mexico. Leaco prides itself on providing state of the art telecommunications services to its members and, as such, is currently planning to offer interstate and international interexchange

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[1](...continued)
Under 47 C.F.R. § 64.1903(a)(3), which has not yet gone into effect, an independent LEC affiliate may take services from its affiliated exchange telephone company not only by tariff, but also on the same basis as requesting carriers that have negotiated interconnection agreements pursuant to Section 251 of the 1996 Act. New rule Section 64.1903 adopted in the *Separate Affiliate Order* has not yet gone into effect. Nonetheless, to the extent necessary, Leaco requests that Section 64.1903 also be waived.

services to its members. Leaco was established in 1954 by a group of customers that realized, if they did not take action, they would have no telephone service. The Tatum Telephone Company, a family owned business, had been served notice long distance service would be discontinued for non-payment. At that time, the Tatum Telephone Company had 200 customers. The customers formed the Cooperative and applied for a Rural Electrification Administration loan in the amount of $331,000 to acquire and continue to operate the telephone company.

Today Leaco has 2,400 members that receive local exchange, intrastate toll, cellular and cable television service as members of the cooperative. The service area started out with less than 25 square miles and today exceeds 7,000 square miles for all services. The growth and services the members receive from the Cooperative are due to one thing; if they do not take the initiative, they cannot receive service from anyone. Stock and commercial companies simply are not interested in investing the capital required to provide service to such a sparsely populated area.

II. **The Separation Requirements Impose an Undue Burden on Leaco and its Members**

The economic impact of a separate affiliate requirement on a small rural telephone cooperative such as Leaco is enormous. As reflected in the Pro-Forma Expense Analysis attached hereto, Leaco would incur expenses in excess of $42,000 in order to establish and maintain a separate affiliate for one year. Almost $21,000 of this expense constitutes costs which would recur annually. This amounts to an annual expense of almost $9.00 per customer served by Leaco *on top of* the $21,800 in one-time start up costs related to the establishment of a separate affiliate. While such costs may simply be considered a cost of doing business for a Regional Bell Operating Company or other large regional carrier, for a small rural telephone cooperative such as Leaco, they impose a significant financial burden, both on the cooperative itself and its members. Indeed, requiring the establishment of a separate affiliate for the provision of interexchange service will make it prohibitively expensive for many Leaco members to take service from Leaco, *thereby depriving them of the ability to take service from the very company they formed enabling them to have service.*

Imposition of a separate affiliate requirement on Leaco would impose other costs as well. In addition to the one-time and recurring costs of creating and maintaining a separate affiliate discussed above, Leaco and its members will incur a significant financial tax burden in the absence of the requested waiver. This unique tax burden stems from Leaco's legal status as a cooperative. Cooperative members are the stock holders of the company and provide equity to increase and improve services. In return for providing equity, they are entitled to capital credits. Capital credits are simply the operating margin of the cooperative. To be able to operate in this fashion, Section 501(c)(3) of the Internal Revenue Code allows all revenue to the cooperative generated by the members to be exempt from federal income tax. Approval of this waiver will allow toll revenues to be considered member generated for those members who choose Leaco as their toll provider. Without the tax exemption, services would have to be priced at rates that most would consider to be very high. As reflected in Leaco's 1996 audit report, a copy of which will be provided upon Commission request, the combined federal and state corporate rates which Leaco would pay should it lose its tax exempt status would have been 42%. Leaco estimates a detrimental annual impact of approximately $38,000 (approximately $16.00 per member) should this waiver be denied. Accordingly, the cumulative financial impact of a separate affiliate requirement on Leaco (assuming all Leaco members selected Leaco as their toll service provider) would amount to over $80,000 during the first year, over $33 per member! A denial of this waiver request will further result in additional expenses of approximately $59,000 per year (and approximately $25 per member) thereafter.[2] Those costs borne by the customer far outweigh any supposed benefits to be derived from application of the separate affiliate requirement to Leaco. The FCC's application of the *Fifth Report and Order's* separate affiliate requirement to independent LECs was based on the underlying assumption that such requirements "are not overly burdensome." *See, e.g.*, Separate Affiliate Order at ¶¶ 165-167. Because this assumption clearly does not apply to Leaco, a waiver of the requirements is consistent with the underlying purpose of the requirements. *See WAIT Radio v. FCC*, 418 F.2d 1153 (D.C. Cir. 1969).

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[2] In addition, numerous interexchange carriers currently charge a monthly service fee if the end user does not make enough calls to justify billing long distance. In most cases the charges are around $5.00. The minimum fee burdens a good number of Leaco's members who are on fixed incomes. These members could avoid such charges by taking service from their cooperative. However, if Leaco is required to establish an affiliate company to provide interexchange services to its members, this will increase the cost of services because of the accounting of two separate companies and the loss of the tax exemption allowed cooperatives.

III. <u>Grant of the Requested Waiver Would Not Implicate the Policy Concerns Underlying the *Fifth Report and Order*</u>

The separate affiliate requirements established in 1984 in the *Fifth Report and Order* were justified by the Commission on the grounds that independent LECs possess market power relative to their service areas and that such requirements were necessary to protect the public against cost-shifting and anti-competitive conduct by the independent LEC. These concerns have no validity with respect to Leaco. Leaco simply will not have the motivation nor the capability to utilize its local exchange or interexchange operations to the benefit of the other. Leaco is regulated by both the FCC and the New Mexico State Corporation Commission. The Commission's own Part 64 rules direct local exchange carriers in how they are to allocate costs between regulated and nonregulated operations. Furthermore, as a local exchange carrier regulated by the New Mexico State Corporation Commission, Leaco cannot raise local rates to subsidize its interexchange operation. The New Mexico State Corporation Commission carefully reviews any local rate increase request and would not approve such a filing without extensive cost support and justification. Finally, as a resale interexchange carrier, Leaco will not be able to obtain any favorable access treatment from its local exchange operations. Leaco's interexchange operation will be paying a fee to its underlying facilities-based carrier, which will in turn pay access to Leaco's local exchange operations. Therefore, any favorable access treatment afforded to Leaco's underlying facilities-based carrier would have to be made available to all other interexchange carriers.

Leaco should be regulated as a non-dominant carrier, without the separate affiliate requirements. This action is entirely appropriate and consistent with the Commission's responsibilities under new Section 10(a) of the Communications Act.[3] Section 10(a) provides the Commission with the duty to forbear from applying any regulation if: (1) the regulation is unnecessary to ensure that charges and practices are just and reasonable; (2) enforcement of such regulation is not necessary for the protection of consumers; and (3) forbearance from applying such provision or regulation is consistent with the public interest. The changes associated with the Telecommunications Act of 1996[4] ensure that an independent LEC, like Leaco, can no longer (if it ever could) behave as a dominant carrier when compared to its competitors in what is increasingly a geographically broad and integrated services marketplace.

Equity dictates that Leaco have the flexibility to compete with national telecommunications service providers that are lightly regulated at the federal level. It is incomprehensible that a global corporate giant like AT&T is regarded as a non-dominant carrier, while Leaco, with only 2,400 member customers, is classified as a dominant carrier.

Therefore, Leaco respectfully petitions the Commission for a waiver of the separate affiliate requirements for non-dominant status as established by the *Fifth Report and Order*. The

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[3] Codified at 47 U.S.C. § 10(a).

[4] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996).

costs imposed on Leaco, its members and its customers by imposition of a separate affiliate requirement far outweigh any illusory perceived benefit to the public stemming from the provision of interexchange service by a separate affiliate. To the extent necessary, Leaco also requests a waiver of Section 64.1903 of the FCC's rules and requests that the Commission forbear from regulating Leaco's interstate domestic and international interexchange service as dominant.

Respectfully submitted,

LEACO RURAL TELEPHONE COOPERATIVE, INC.

John Smith

John Smith
Executive Vice President/General Manager

Date: 8-12-97

Leaco Rural Telephone Cooperative, Inc.
Pro Forma Expense Analysis
Incremental Expense Required to Create and Maintain Affiliate

Non-recurring Cost

Legal and Incorporation Cost	$ 3,000
Accounting Start-up	800
Computers and Software Upgrade	18,000
	$21,800

Recurring Cost (Annually)

Accounting	$ 9,600
Separate Billing for IXC Service	5,000
Audit	2,000
Board Expense	1,500
Building Lease	1,000
Communications Expense	600
Advertising	1,000
	$20,700

TOTAL COSTS (Year One)	**$42,500**

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